Supreme Court of the United States

OCTOBER TERM 1940.

No. 323

AMERICAN NATIONAL BANK OF NASHVILLE, TENNESSEE,

Petitioner.

versus

CITY OF SANFORD, FLORIDA, ET AL.

Brief on Behalf of American National Bank of Nashville, Tennessee, Petitioner, for Writ of Certiorari to the United States Circuit Court of Appeals, Fifth Circuit.

GEORGE W. WYLIE,
STUART B. WARREN,
F. A. BERRY,
J. BLANC MONROE,
MONTE M. LEMANN,
Attorneys for Petitioner.

WYLIE & WARREN,
BASS, BERRY & SIMS,
MONROE & LEMANN,
Of Counsel.

August, 1940.

INDEX TO BRIEF

TABLE OF CASES

TABLE OF CASES—Continued

Supreme Court of the United States

OCTOBER TERM 1940.

No.

AMERICAN NATIONAL BANK OF NASHVILLE, TENNESSEE,

Petitioner.

versus

CITY OF SANFORD, FLORIDA, ET AL.

Brief on Behalf of American National Bank of Nashville, Tennessee, Petitioner, for Writ of Certiorari to the United States Circuit Court of Appeals, Fifth Circuit.

I. *RELIEF SOUGHT*

This brief is filed in support of the petition of American National Bank of Nashville, Tennessee, for a certiorari to the United States Circuit Court of Appeals, Fifth Circuit, to review its judgment rendered May 31, 1940, (R. 165-172), rehearing refused July 8, 1940, 112 Fed. (2d) 435, affirming an order of the United States District Court for the Southern District of Florida (R. 153).

II. *BASIS OF JURISDICTION OF THIS COURT*

The jurisdiction of this Court is asserted under Judicial Code §204 and §262, as amended, U.S.C.A. Title 28,

Section 347 and 377; Chapter IV, Sec. 24(c) Bankruptcy Law, as amended (Chandler Act) U. S. C. A. Title 11, Sec. 47, and Rule 38 of this Court.

239 U. S. 11, *Central Trust v. Lueders.*
191 U. S. 115, *Holden v. Stratton.*

III. *CONCISE STATEMENT OF CASE*

After the first Municipal Bankruptcy Act had been declared unconstitutional and before the adoption of the present Municipal Bankruptcy Act, or Section 83(j) thereof, the City of Sanford (R. 23) offered to any of its bondholders willing to accept same, regardless of acceptance or rejection by others a **plan of voluntary adjustment** under which the accepting bondholders were to surrender and cancel their "old bonds" and coupons and accept new bonds, having materially different rights. This plan was not and could not have been a composition under the Bankruptcy Act, but was a ***voluntary adjustment plan.*** Some 87% of the bondholders accepted this offer, surrendered and cancelled their "old bonds" and accepted new bonds for scaled-down amounts (R. 3, 7). The restoration of these bondholders to the *status quo ante* was prohibited (1) by the Florida law, (2) by the decisions of the Supreme Court of Florida, (3) by the charter of the City of Sanford and (4) by the **voluntary adjustment plan** (Vid. *infra*, p. 5). Unfortunately the Circuit Court of Appeals fell into error on this point and believed erroneously that the Florida law permitted the restoration to the *status quo ante* (Vid. *infra*, p. 8). Thus at the date of the adoption by Congress of the second Municipal Bankruptcy Act, the municipal indebtedness of the City of Sanford really consisted of two series of bonds,—**first,** outstanding "old bonds" and **second,** outstanding "refunding bonds". The rights of the two series were materially different.

With its indebtedness in this position, the City of Sanford, after the adoption of the second Municipal Bankruptcy Act (Chandler Act) and after the adoption of the amendment thereof contained in Section 83(j) *supra*, filed a petition (R. 1-81, incl.) for a composition of its debt under Chapter X of the Bankruptcy Act (Chandler Act). This **plan of composition** did not propose to change in any manner whatever the rights of the holders of the "refunding bonds" as they then existed, but did propose to change matrially the rights of the holders of the "old bonds", who had refused to refund. The Chandler Act[1] requires the bankruptcy petition to show that the creditors of the petitioner owning not less than 51% in amount of the securities **affected by the plan** have accepted it in writing. The City of Sanford in an effort to meet this jurisdictional prerequisite, attached to its petition the written consents of a large number of the holders of "refunding bonds". By stipulation, only one such consent has been printed. (R. 82). The consents so obtained do not amount to 51% of the non-assenting **"old bondholders"** who **are** materially affected by the plan (not one single non-assenting old bondholder has consented), but they do amount to 51% of the total outstanding bonded indebtedness, including the holders of

(1) The Chandler Act contains the following provisions:
USCA Title 11, §402

"The term 'security affected by the plan' means a security as to which the rights of its holder are proposed to be adjusted or modified materially by the consummation of a composition agreement."

§403:

"The petition shall state that a plan of composition has been prepared, is filed and submitted with the petition, and that creditors of the petitioner owning not less than 51% in amount of the securities affected by the plan (excluding, however, any such securities owned, held or controlled by the petitioner), have accepted it in writing. * * *

"No creditor shall be deemed to be affected by any plan of composition unless the same shall affect his interest materially, and in case any controversy shall arise as to whether any creditor or class of creditors shall or shall not be affected, the issue shall be determined by the judge, after hearing, upon notice to the parties interested."

the "refunding bonds" who **are not** at all affected by the plan, and the holders of the **"old bonds"** who **are** materially affected by the plan. The City of Sanford contended that this petition was made legally sufficient by the provisions of the amendment contained in 83(j) of the Bankruptcy Act.[1]

To this petition, the American National Bank, petitioner herein, and two other non-assenting bondholders made timely objection, challenging the sufficiency of the petition as a matter of law, asserting that the consent of 51% of the creditors materially affected by the plan was jurisdictionally essential but had not been given or averred, and asserting that Section 83(j) of the Bankruptcy Act was not applicable, and if held applicable, was unconstitutional. The Attorney General of the United States was notified and his office filed a brief and made an oral argument herein. The Bank moreover asserted (R. 109, *et seq.*) that it was the holder of more than 50% of the unrefunded or **"old bonds"**, which alone were affected by the proposed plan,[2] that it had not consented to the plan. The prayer was that the City's petition should be dismissed for failure to show, as required by the statute, that the 51% of the securities affected by the plan had accepted it in writing. This application to

(1) 83(j):

"The partial completion or execution of any **plan of composition** as outlined in any petition filed under the terms of this title by the exchange of new evidences of indebtedness under the plan for evidences of indebtedness covered by the plan, whether such partial completion or execution of such **plan of composition** occurred before or after the filing of said petition, shall not be construed as limiting or prohibiting the effect of this title, and the written consent of the holders of any securities outstanding as the result of any such partial completion or execution of any **plan of composition** shall be included as consenting creditors to such **plan of composition** in determining the percentage of securities affected by such **plan of composition.**"

(2) Petitioner's claim was for $152,000 and the total unscaled and unrefunded old bonds outstanding amounted to the principal sum of $246,000.

dismiss, after hearing before a Master, was denied by the District Court (R. 153) and from the affirmance of this decree by the Fifth Circuit Court of Appeals (112 Fed. (2d) 435) this application for certiorari is prosecuted.

IV. *ASSIGNMENTS OF ERROR*

(1) The Court of Appeals erred in holding that "nothing in the acceptance (of the plan of voluntary adjustment) prevents the City and the acceptors from undoing the whole plan", since (a) the statutes of Florida, (b) the decisions of the Supreme Court of Florida, (c) the City charter of Sanford, and (d) the express provisions of the "plan of voluntary adjustment", all prohibit restoration of the *status quo ante.*

(2) The Court of Appeals erred in holding that Section 83(j) of the Municipal Bankruptcy Act is applicable not only to a partially completed **"plan of composition"**, but also to a partially executed **"plan of voluntary adjustment"**, although said **"plan of voluntary adjustment"** was (a) executed irrevocably by a large majority of the bondholders at a time when there was no Municipal Bankruptcy Act in existence; (b) did not contemplate submission to or approval by any Court; (c) contemplated no coercion of non-assenting minority bondholders; and (d), did not contemplate collective action, but was offered to and accepted by individual bondholders, each being permitted to act and acting finally and irrevocably for himself, regardless of the action of the other bondholders.

(3) The Court of Appeals erred, as a matter of law, in failing to hold that holders of "old bonds" and holders of "refunding bonds" are in different classifications and hence consents of one class may not be used to coerce

members of the other class, although the Supreme Court of Florida, 193 So. 297, *State ex rel Garland v. City of West Palm Beach* has expressly held that they are payable from different funds and although Sec. 83(b) as amended by the Act of Congress approved June 28, 1940, expressly requires such separate classification.

(4) The Court of Appeals erred in ruling that the written acceptances of holders of "refunding bonds" who are in no wise affected by the **"plan of composition"** can be considered in computing the 51% of acceptances required by the Municipal Bankruptcy Act, §83(a); (11 U. S. C. A. §403).

(5) The Court of Appeals erred in ruling that holders of "old bonds", being creditors of a class whose rights are materially adversely affected by a proposed **"plan of composition"**, may be coerced into accepting that **"plan of composition"** by holders of "refunding bonds", being creditors of a different class, whose rights are in no wise affected by the proposed **"plan of composition"**.

(6) The Court of Appeals erred in failing to hold (a) that if the plan sought to be confirmed was the plan of February 1, 1937 (R. 23), it was not a plan of composition within the meaning of the Bankruptcy Act or of Section 83(j); (b) that if the plan was the plan of January 28, 1939 (R. 1), the holders of the "refunding bonds" were not creditors affected by the plan, and their consents cannot be used to coerce creditors who are affected by the plan and who are in a different classification.

(7) The Court of Appeals erred in holding that Section 83(j) of the Bankruptcy Act (U. S. C. A. Title 11, §403(j) should be construed as having retroactive

application to securities received and rights abandoned before its adoption.

(8) The Court of Appeals erred in failing to hold that if Section 83(j) of the Bankruptcy Act be construed as applicable to the case at bar and as authorizing creditors, whose rights are unchanged by a **"plan of composition"**, to compel acceptance of that plan by creditors whose rights are materially curtailed by that plan, it is null and void as being in violation of the provisions of the Federal Constitution, particularly Amendment V.

Assignment No. (1).

> The Court of Appeals erred in holding that "nothing in the acceptance (of the plan of voluntary adjustment) prevents the City and the acceptors from undoing the whole plan", since (a) the statutes of Florida, (b) the decisions of the Supreme Court of Florida, (c) the City charter of Sanford, and (d) the express provisions of the "plan of voluntary adjustment", all prohibit restoration of the *status quo ante.*

The Court of Appeals in its opinion (R. 165), 112 Fed. 437 and 439, said:

Page 438:

> "Nothing in the acceptance prevents the City and the acceptors from undoing the whole plan."

Page 437:

> "If the City and the assenting bondholders, because of failure to secure full consenting, concluded to revoke the plan and restore the bonded indebtedness to its original condition, it could hardly be contended, we think, that appellant

could assert a vested right to prevent their doing so."

In so holding, the Court is in direct conflict with:

(1) The statutes of the State of Florida,

(2) The decisions of the Supreme Court of the State of Florida,

(3) The City charter of the City of Sanford, and

(4) The express provisions of the plan of voluntary adjustment.

Thus:

(1) The Florida statute under which the **"refunding bonds"** were issued, namely, Chapter 15,772 of the Laws of Florida, 1931, Section 8, permits bonds to be exchanged: (See Appendix, p. 46).

> "for not less than an equal principal amount and for accrued interest of debts to be retired thereby",

and Section 14 provides that:

> "The principal and accrued interest of the refunding bonds shall not exceed the amount of the obligations refunded."

Therefore, when the 87% of the bondholders accepted **"refunding bonds"** for the scaled-down amounts, which they did irrevocably and unconditionally, thereby becoming creditors of the City of Sanford for the scaled-down amounts only, they were precluded from being reinstated as creditors for the original and larger amounts, since in order to reinstate them, any **"refunding bonds"** given them would necessarily be for a sum which would "exceed the amount of the obligations refunded."

(2) The Supreme Court of the State of Florida, in the case of *City of Miami vs. State*, 190 So. 774, said:

> "To prevent an unlawful indebtedness, no interest coupons shall be paid or left on bonds exchanged or sold by the municipality, except for interest at the bond rate from the date of the exchange or of the sale, payment and delivery of the refunding bonds; and interest on the refunded bonds should be paid only to the date of the exchange or of the purchase and delivery of the bonds for redemption; and there should be cancelled and retired all interest coupons except the current coupons on refunding bonds prior to the date of exchange or to the payment for the sale and delivery of the refunding bonds. Interest to the date of exchange or to sale, payment and delivery, represented by current coupons on the refunding bonds when they are exchanged or delivered on sale and payment, should be credited on the current coupons at delivery. When bonds are purchased for redemption, cancellation and retirement, interest thereon should be paid only to the date of delivery; and all current and future interest coupons that should be thereon, should be delivered with the refunded bonds, and both bonds and coupons should be duly listed of record and canceled and permanently retired from circulation or any other use whatever."

In the present instance, the **original bonds** were surrendered in exchange for **"refunding bonds"** by the 87% of the bondholders, and **"refunding bonds"** disclaiming past due interest and bearing future interest at a different rate were accepted unconditionally by them. Under the ruling of the Court, the original bonds were required to be "cancelled and permanently retired from circulation or any other use whatever".

(3) The charter of the City of Sanford, Chapter

9897 of the Laws of Florida, 1923, Special Acts Vol. 2, contains as Section 123 a section reading as follows:

> "Section 123. The City Commission in its corporate capacity is authorized to issue from time to time bonds of the City of such denominations, bearing such rate of interest, not to exceed six (6) per cent, and becoming due in such time and upon such conditions as may be determined, for any and all municipal purposes mentioned in this Act, and for such other lawful municipal purposes as may be determined by Ordinance; provided, however, that (except as otherwise provided in this Act) before the issue of any bonds shall be made, an ordinance shall be passed expressing in exact terms the amount of the bond issue and purpose for which such monies to be realized are to be used, which said ordinance proposing the issue of bonds shall subsequently be approved by a majority vote of the electors of the City, who are qualified to vote, as shown by the registration books of the City, voting at an election held for that purpose, at such time and in such manner as may be prescribed by law, and the City ordinances; and, provided further, that the aggregate issue of bonds outstanding and unpaid shall at no time exceed fifteen (15) per cent of the assessed valuation of the real and personal property of the municipality, as shown by the assessment roll of the municipality. The question of the issuance of bonds for any specific purpose may be submitted from time to time, not oftener than once each year, with relation to each purpose specified."

This *per se* would prevent a reconstitution or restoration of the old indebtedness.

(4) The City of Sanford's voluntary adjustment offer (R. 23, *et seq.*) provides in part:

R. 41:

> "Section 6. Upon delivery of the refunding bonds in exchange for outstanding bonds, all past due coupons, if any, shall be detached from the refunding bonds and cancelled by the City, and all unmatured coupons shall be attached thereto."

This was done.

R. 46:

> "Section 15. The refunding bonds authorized hereby when executed shall be delivered to the holders of the outstanding bonds to be refunded thereby and/or the holders of judgments thereon in exchange for and upon surrender of an amount of such bonds and/or the satisfaction of any judgment obtained upon a principal amount of such bonds equal to the face amount of the refunding bonds exchanged therefor."

This was done, and when the City of Sanford (R. 1, *et seq.*) filed its **plan of composition,** it listed the "refunding bonds" not at the amount of the "old bonds", but at the scaled-down amount of the "refunding bonds."

Moreover, the City of Sanford's resolution adopted after the passage by Congress of the second Municipal Bankruptcy Act is in the Record, 75, *et seq.*, and provides:

R. 75:

> "Whereas, on the first day of February, 1937, the City of Sanford, Florida, had outstanding debts in the principal amount of $5,900,000, evidenced by bonds and judgments, * * * and on said 1st day of February, 1937, adopted a plan * * * which said plan was embodied in resolution No. 499 * * * and which resolution provided that said refunding bonds, Series A, should be issued in exchange for the principal of all of the outstanding

bonds of said City of Sanford * * *.

"Whereas, said plan * * * has been partially completed by the exchange of refunding bonds of Series A.

* * * * *

"Whereas, said City of Sanford now has outstanding the aforesaid refunding bonds, Series A, in the aggregate principal sum of $4,923,000 and the aforesaid refunding bonds, Series B, in the aggregate principal sum of $593,000, and the aforesaid bonds in the aggregate principal sum of $250,000, hereinbefore particularly described and which have not been exchanged for refunding bonds."

The petition of the City of Sanford to the Bankruptcy Court recites, R. 3:

"and said plan of composition was accepted by the holders of all of petitioner's said bonded indebtedness except the holders of the bonds hereinafter specifically described, and pursuant to the terms of said plan of composition adopted on the 1st day of February, 1937, petitioner has exchanged the aforesaid refunding bonds, Series A, for all of petitioner's bonded indebtedness except the following:"

(Here follows a list of the non-assenting bonds).

Page 7:

"Petitioner further respectfully shows and represents unto the Court that it has a total outstanding indebtedness consisting of refunding bonds, Series A, in the principal sum of $4,908,000, bearing interest as aforesaid, and a total outstanding indebtedness consisting of refunding bonds, Series B, in the principal sum of $593,000, bearing interest as aforesaid, and the aforesaid bonded indebtedness hereinbefore particularly described for which refunding bonds,

Series A and B, have not been exchanged, amounting to the principal sum of $231,000 of bonds, for which refunding bonds, Series B, may be exchanged; that all of the aforesaid bonds are general obligations of petitioner".

It appears from the foregoing that the Court of Appeals "has decided an important question of local law in a way probably in conflict with applicable local decisions", and that under Rule 38(b) of this Honorable Court, a certiorari should issue. The point is of grave importance, since it is the only basis upon which holders of refunded bonds can possibly claim any interest in the plan of January 28, 1939.

Assignment No. (2).

The Court of Appeal erred in holding that 83(j) of the Municipal Bankruptcy Act is applicable not only to a partially completed **plan of composition**, but also to a partially executed **plan of voluntary adjustment**, although said **"plan of voluntary adjustment"** was (a) executed **irrevocably** by a large majoritty of the bondholders at a time when there was no Municipal Bankruptcy Act in existence; (b) contemplated no coercion of non-assenting bondholders; (c) contemplated no submission to or approval by any Court; and (d) did not contemplate collective action, but was offered to and accepted by individual bondholders, each being permitted to act and acting finally and irrevocably for himself, regardless of the action of the other bondholders.

Section 83, U. S. C. A. Title 11, paragraph 403, (j), reads:

> "The partial completion or execution of any **PLAN OF COMPOSITION** as outlined in any petition filed under the terms of this title by the exchange of new evidences of indebtedness under the plan for evidences of indebtedness covered by the plan, whether such partial completion or execution of such **PLAN OF COMPOSITION** occurred before or after the filing of said petition, shall not be construed as limiting or prohibiting the effect of this title, and the written consent of the holders of any securities outstanding as the result of any such partial completion or execution of any **PLAN OF COMPOSITION** shall be included as consenting creditors to such **PLAN OF COMPOSITION** in determining the percentage of securities affected by such **PLAN OF COMPOSITION.**" (Emphasis by present writers).

The Court can not fail to observe how meticulously careful the lawmakers were in confining the application of Section 83(j) to a **"plan of composition"**. This meticulous care was undoubtedly due, in part, at least, to the fact that this Court had set aside in the *Ashton* case, 298 U. S. 513, the original Municipal Bankruptcy Act, which was bottomed on the general bankruptcy powers, and had affirmed in the *Bekins* case, 304 U. S. 27, the constitutionality of the second Municipal Bankruptcy Act, which was expressly bottomed on the **composition power.** Thus, the second sentence of the opinion of this Court reads:

> "They present the question of the constitutional validity of the Act of August 16, 1937, 50 Stat. 653, amending the Bankruptcy Act by adding Chapter 10, providing for **the composition of indebtedness** of the taxing agencies or instrumentalities therein described." (304 U. S. 45).

The *Ashton* case, which held the original Municipal Bankruptcy Act unconstitutional, was decided May 25, 1936. Congress adopted the second Municipal Bankruptcy Act on August 24, 1937 (50 Stat. 653) and amended same by adding Section 83(j) on June 22, 1938 (52 Stat. 940). As appears from R. 2, the City of Sanford on February 1, 1937, **that is to say, at a time when the old Municipal Bankruptcy Act had been declared unconstitutional and the new Municipal Bankruptcy Act had not as yet been passed,** adopted a **plan of voluntary adjustment** of its indebtedness, which was evidenced by resolution No. 499, adopted by the City Commission on the 1st day of February, 1937, and which is set out *in extenso*, on pages 23, *et seq.* of the Record. This plan was not and could not have been a **plan of composition** under the Municipal Bankruptcy Act for the following reasons:

(1) At the time that it was propounded to and accepted by the large majority of the outstanding bondholders, there was no Municipal Bankruptcy Act in existence, and therefore, it necessarily could not have been a **plan of composition** under a Bankruptcy Act.

(2) That plan contemplated no submission to, or approval by any court.

(3) That plan contemplated no coercion of non-assenting minority bondholders by any court or by any other authority.

(4) That plan did not contemplate collective action, but expressly authorized any individual bondholder to surrender his "old bonds" and receive his "refunding bonds" regardless of any action which any other holder or holders of "old bonds" might or might not take; and as a matter of fact, some 87% of the holders of the "old bonds" surrendered their "old bonds" and received "refunding bonds". The "old bonds" were thereupon can-

celled and the new "refunding bonds" recognized as the existing obligations of the City,—so much so, that when the City subsequently, on January 28, 1939, R. 1, filed its petition in Bankruptcy and its **plan of composition,** it set up not the "old bonds," but the "refunding bonds" as its outstanding obligations.

From this it is at once apparent that the "refunding bonds" were not and are not "securities outstanding as the result of any such partial completion or execution of any **plan of composition**", as required by Section 83(j).

A "plan of composition" has a well-defined and special meaning in bankruptcy parlance, which fact has been repeatedly recognized.

96 Fed. (2d) 85, *In re: City of West Palm Beach:*

> "The Municipal Bankruptcy Act speaks uniformly of a **'plan of composition'.** In bankruptcy matters, composition has a special meaning, to-wit, a settlement or adjustment which is enforced by the court on all creditors after its acceptance by a required majority. A proposed adjustment out of court is not a plan of composition, but may become one by being presented to the court. That the present adjustment was proposed and largely accepted before the Act was passed and of course not as a plan of composition, would, if it remained executory, possibly not prevent its presentation for enforcement under the Act. * * * Whether the plan must have been offered and accepted as a plan of composition rather than as a plan of voluntary adjustment we need not decide since the plan with its acceptance became incapable of presentation as a composition, because it had been largely executed."

8 *Corpus Juris Secundum*, Bankruptcy, Section 653:

> "A composition had in accordance with the

Bankruptcy Act, Section 12 (11 United States Code Annotated, Section 30) partakes of the nature of a bargain or settlement in the **nature of a contract approved by the court,** originating usually in an offer for the debtor and resulting in the main from voluntary acceptance by a majority of the creditors, whereby the debtor agrees with his creditors to release his property from creditors' claims and secure his own discharge in return for the payment of a specified sum to be distributed ratably among the general creditors, and such sum as may be necessary to pay priority claims and costs of the proceedings. To be within the provisions of the Bankruptcy Act, the composition must be entered into by one against whom a voluntary or involuntary petition has been filed or who has been adjudged a bankrupt."

In re Merriman, 17 Fed. Cas. No. 9479:

"The differences are radical between the nature of a composition *inter partes* and of a bankruptcy composition. The root of their differences is the fact that the entire proceedings for and in a bankruptcy composition are proceedings in bankruptcy, and are a part of a system for the compulsory division of assets which is administered by a court, while a composition *inter partes* derives its validity merely from the will of the parties. These differences induced the Supreme Court of Massachusetts to declare recently that the proceedings for a composition under the statute 'differ wholly in nature and effect from a voluntary composition which binds only those executing it.' *Guild v. Butler,* (Oct., 1877) (122 Mass. 498)."

In re Bickmore Shoe Company, 263 Fed. 926:

"It cannot be successfully maintained that a composition is not a part of the bankruptcy pro-

cedure. While it depends for its effect upon an acceptance by a majority in number and amount of the creditors, it is only of 'creditors whose claims have been allowed.' Section 12b. The allowance is itself court action. The composition is of no avail, unless confirmed by the court after a judicial hearing. It results, not alone in a contract between those who have assented, but in a judgment imposing its terms upon those who have not assented, and establishes consequences declared by the law independent of stipulation in the contract, such as that the title to the bankrupt's property shall revest in him, and that a discharge from his debts, with fixed exceptions, shall result.

> " 'The composition proceeding is therefore a part of the proceeding in bankruptcy, and one of the modes which the bankrupt law authorizes of releasing the debtor and securing to his creditors an equal share of his means. * * * As we have * * * said, these several statutes, sections, and provisions are to be construed as parts of one entire system of bankrupt law.' "

In the case of *First National Bank of St. Albans v. Wood*, 53 Vt. 491, the court held that a composition agreement was part of the proceeding in bankruptcy, and stated:

> "The grounds of distinction between this case and that of an ordinary compromise agreement between debtor and creditors as in *Paddleford v. Thacher*, 48 Vt. 574, are numerous and obvious.
>
> "The latter is a proceeding not in court, or the subject of judicial determination before its validity is established, but rests purely in contract and is dependent upon the agreement of creditors, their mutual promises as between each other constituting the consideration of each. A creditor votes to accept a proposition of composi-

tion in bankruptcy, not upon condition that all the other creditors will do the same, but because he believes he will get more money on his debt by a settlement under the composition provisions of the statute than through the intervention of an assignee. There is no consideration for his vote. It is simply his expression of preference as between two methods of settlement of the estate, the action of the court being alike necessary to effectuate either. An affirmative vote of all creditors is not required in any case; and if all vote affirmatively the court is not necessarily bound by it, but it 'may refuse to accept or confirm the composition.' * * * It is the action of the court that finally operates the discharge, and there would be none without such action."

Assignment No. (3).

The Court of Appeals erred as a matter of law in failing to hold that holders of "old bonds" and holders of "refunding bonds" are in different classifications and hence consents of one class may not be used to coerce members of the other class.

There is no controversy as to the facts in this matter. The record affirmatively shows (R. 23, *et seq.*) that on February 1, 1937, the City of Sanford adopted a resolution propounding a plan for the **voluntary adjustment** of its bonded indebtedness. That plan was offered to each bondholder as an individual and under it, each bondholder was entitled to surrender his "old bond" for cancellation and to accept irrevocably his new bond. At R. 27 and 28, it affirmatively appears that the new bondholder surrendered his claim to past due interest which had accrued prior to March 1, 1937, and agreed to accept for the future a different and reduced schedule of inter-

est. It moreover appears from the decision of the Supreme Court of Florida in the case of *State ex rel Garland v. City of West Palm Beach*, 193 So. 297, a case arising under this same Chapter 15,772 of the Acts of 1931, that that Court expressly held that the holder of "old bonds" who refused to exchange them for new bonds could not insist upon the payment of the principal and interest thereon from moneys in the sinking fund provided for the payment of the principal and interest of the new bonds, since that was a special fund dedicated to the payment of the new bonds. This clearly demonstrates that the rights of the holders of the **"old bonds"** are materially different from the rights of the holders of the **"refunding bonds"**, and that the two sets of bonds are necessarily in separate classifications. Headnote No. 1 to that decision reads

> "1. Municipal corporations—951
> Where City of West Palm Beach issued refunding bonds for purpose of exchange and to take place of outstanding bonds which were supported by a tax levy sufficient to pay them as they matured, and refunding bonds were supported by a sinking fund, a holder of outstanding bonds who refused to exchange them for refunding bonds could not enforce payment of principal and interest of outstanding bonds from money held in the sinking fund created for the refunding bonds. Acts 1931, Ex. Sess., c. 15772; Sp. Acts 1933, c. 16758."

When this is compared with the language of the amendment to Section 83(b), which is embodied in the Act of Congress approved June 28, 1940, and reported in U. S. Code Congressional Service Advance Sheets No. 6, at page 655, and which reads as follows:

> "Provided, however, That the holders of all claims regardless of the manner in which they are

> evidenced, which are payable without preference out of funds derived from the same source or sources, shall be of one class. The holders of claims for the payment of which specific property or revenues are pledged, or which are otherwise given preference as provided by law, shall accordingly constitute a separate class or classes of creditors."

the error into which the Circuit Court of Appeals fell in failing to hold that the two sets of bondholders are in different classifications is emphasized.

As the class of refunding bondholders is separate and distinct from the class of old bondholders, and as the right of the "refunding bondholders" remain unaffected by the plan, whereas the rights of the "old bondholders" are materially reduced by the plan, the use of the consents of the "refunding bondholders" to coerce the "old bondholders" would be a denial of due process.

Assignment No. (4).

> The Court of Appeals erred in ruling that the written acceptances of holders of "refunding bonds" who are in no wise affected by the **"plan of composition"** can be considered in computing the 51% of acceptances required by the Municipal Bankruptcy Act, Section 83(a); (11 U. S. C. A. §403).

The Municipal Bankruptcy Act contains the following provisions:

U. S. C. A. Title 11, §402:

> "The term **'security affected by the plan'** means a security as to which the rights of its holder are proposed to be adjusted or modified materially by the consummation of a composition agreement."

§403:

> "The petition shall state that a plan of composition has been prepared, is filed and submitted with the petition, and that creditors of the petitioner owning **not less than 51% in amount of the securities affected by the plan** (excluding, however, any such securities owned, held or controlled by the petitioner), have accepted it in writing. * * *
>
> "No creditor shall be deemed to be **affected by any plan of composition unless the same shall affect his interest materially,** and in case any controversy shall arise as to whether any creditor or class of creditors shall or shall not be affected, the issue shall be determined by the judge, after hearing, upon notice to the parties interested."

There is no dispute about the fact that the "refunding bonds" are not affected in the least by the plan propounded by the petition (R. 1) filed January 28, 1939. That plan simply proposes that the **"old bonds"** be scaled down to the level of the **"refunding bonds"**. The consents which were attached to the petition filed January 28, 1939, were all consents by holders of **"refunding bonds."** Not a single **"old bond"** has consented to the plan. Permitting these consents to be considered in computing the 51% of acceptances required by the statute thus quoted is in direct violation of the provisions of the statute, since they are not in any wise **affected by the plan,** and the statute is specific in its requirement that the consents shall be consents of creditors affected by the plan.

96 F. (2d) 85, *In re City of West Palm Beach,* (C. C. A. 5th):

> "It appears from the petition that more than a majority of the floating debts involved in the plan had been exchanged for new funding bonds and about five-sixths in amount of the old bonds had been exchanged for new bonds. The owners of these were no longer acceptors of an executory

plan, but had been fully settled with under it and no longer had any direct interest in it. They could not fairly be counted as voters before the court on the propriety of the plan. Of course they would wish the non-acceptors to be forced to scale their debts as they themselves had done. They could no longer have an open mind as to whether, in the light of developments, the plan was a good one or a bad one. The binding of a minority by a majority having the same interests was discussed as respects corporate reorganizations in Texas Hotel Securities Co. v. Waco Development Co., 5 Cir., 87 F. 2d 395, and Continental Ins. Co. v. Louisiana Oil Ref. Corp., 5 Cir., 89 F. 2d 333. The importance of identity of interest is there stressed. We do not think the creditors of West Palm Beach who have already irrevocably scaled their debts can be counted either in the two-thirds finally to be needed, nor as preliminary acceptors of the scaling plan offered as a composition."

87 F. (2d) 395, *Texas Hotel Co. v. Waco Dev. Co.*, (C. C. A. 5th):

This was a case arising under Section 77 (b) of the Bankruptcy Act, but the provisions of 77(b) concerning classification are similar to the provisions in the Sections before the Court. The Fifth Circuit Court of Appeals said:

> "The right to vote on a plan is not a fixed incident of every allowed claim, but exists **only when its class is affected by the plan** and may vary as the plan is changed or modified."

82 F. (2d) 186, *in re: Nine North Church Street*, (C. C. A. 2nd), the Court said:

> "Before the debtor came into existence, some of the certificateholders had consented to a reduction of their rights. The plan as proposed by the

debtor did not further reduce these modified rights, while it did cut down the rights of those who had not cooperated in Gedex' proposition. Either there were two classes of creditors, with no consents from the second class (as required by §77B (e) (1), 11 U. S. C. A. §207, (e) (1), or there was a single class of creditors, with no reduction made in the rights of some of these, those certificateholders whose rights were already modified."

109 F. (2d) 313, *St. Louis Union Trust Co. v. Champion Shoe Machinery Co.*, (C. C. A. 8th):

"It can be argued that, since all bonds were secured by the same pledged assets under the same trust indenture, the court below had the discretion to place all of the bondholders in a single class for purposes of reorganization proceedings, and that the appellants' only just complaint is against the plan adopted. See and compare, In re Palisades-on-the-Desplaines, 7 Cir., 89 F. 2d 214, 217; J. P. Morgan & Co. v. Missouri Pac. R. Co., 8 Cir. 85 F. 2d 351, 352. We think that the appellants' rights were sufficiently distinct from those of other bondholders to entitle the appellants and those who were similarly situated to a separate classification. See Gerdes, Corporate Reorganization, 1936, Vol. 2, §§1045-1046, pp. 1681-1682; Finletter, Principles of Corporate Reorganizations, pp. 423-424. Whether the appellants be regarded as entitled to payment before other bondholders may have recourse to the pledged assets, or as having a lien on the pledged assets superior to that of other bondholders, we think is not important. The rights of the bondholders who consented to the last extension were, by the terms of the trust indenture, subordinated to the rights of those who never consented to any extension and to the rights of those who consented only to the first extension.

Agreements of creditors to subordinate their indebtedness to that of other creditors will be given effect in bankruptcy proceedings. Bird & Sons Sales Corporation v. Tobin, 8 Cir., 78 F. 2d 371, 373, 100 A. L. R. 654, and cases cited.

"The record shows that the bonds of the appellants and of others in their situation and the bonds of those who never consented to any extension were fully secured by the assets pledged; that other bonds evidently were not; that under the plan of reorganization, which made no distinction between bondholders, the appellants and the others whose rights are superior to those of other bondholders will not receive the worth of their bonds. The plan which compels them to surrender, without adequate consideration and for the benefit of other bondholders, the superior rights which they acquired is inequitable and unfair. See and compare, In re Nine North Church Street, Inc., 2 Cir., 82 F. 2d 186; Sophian v. Congress Realty Co., 8 Cir., 98 F. 2d 499; Case v. Los Angeles Lumber Products Co., 308 U. S. 106, 60 S. Ct. 1, 84 L. Ed. ___."

89 F. (2d) 214, *In re Palisades-On-The Desplaines*, (C. C. A. 7th):

The Court said at page 217:

"There is much in appellant's contention to commend it to our serious consideration. His position is based upon the interpretation of that part of the statute here involved, by Mr. Gerdes in his work on Corporate Reorganization (1936), vol. 2, §1046, p. 682:

" 'All creditors of equal rank with claims against the same property should be placed in the same class. This is natural, logical, and a simple basis of division.

" 'Conversely, creditors of different ranks, or creditors of the same rank but with claims against different properties, should be placed

> in different classes. The owners of a mortgage which is a first lien on certain property should be in a class other than one containing the owners of a mortgage which is a second lien on the same property. So, also, the holders of a mortgage, which is first lien on certain property should be in a class other than the one containing the holders of a mortgage which is a first lien on other property."

85 F. (2d) 351, *J. P. Morgan & Co. v. Missouri-Pac. R. Co.*, (C. C. A. 7th):

This was a bankruptcy proceeding under the Railroad Section 11 U. S. C. A. §205, and the Circuit Court of Appeals of the Eighth Circuit held:

> "We agree with this statement of the District Court, and it follows that the classification should in no wise depend upon the nature of the claimant or his interest in the sense of his bias or leanings, but only upon the nature of the claim."

See also *Continental Insurance Co. v. La. Oil Refining Corp.*, 89 F. (2) 333.

Assignment No. (5).

> The Court of Appeals erred in ruling that holders of "old bonds", if creditors of a class whose rights are materially adversely affected by a proposed **"plan of composition"** may be coerced into accepting that **"plan of composition"** by holders of "refunding bonds", creditors of a different class whose rights are in no wise affected by the proposed **"plan of composition"**.

As stated *supra* and as demonstrated by the record,

the **"plan of composition"** filed January 28, 1939, contemplates a shrinkage in the claims of the holders of **"old bonds"**. It does not contemplate any change in the status of the **"refunding bonds"**.

The statute (11 U. S. C. A. §402 and 403) provides:

> "§402. The term 'security affected by the plan' means a security as to which the rights of its holders are proposed to be adjusted or modified materially by the consummation of a composition agreement."
>
> "§403: The petition shall state that a plan of composition has been prepared, is filed and submitted with the petition, and that creditors of the petitioner owning not less than 51% in amount of the **securities affected by the plan** (excluding, however, any such securities owned, held or controlled by the petitioner), have accepted it in writing. * * *
>
> "No creditor shall be deemed to be affected by any plan of composition unless the same shall affect his interest materially, and in case any controversy shall arise as to whether any creditor or class of creditors shall or shall not be affected, the issue shall be determined by the judge, after hearing upon notice to the parties interested."

These provisions meticulously guard creditors affected by the plan against coercion by creditors of a different class who are not affected by the plan. The point is fundamental in its importance. In a composition coercion can be exerted only by parties whose interest is affected upon parties whose interest is also affected in substantially the same way. Any other form of coercion is beyond the scope of a composition and by a comparison of the *Ashton* case (298 U. S. 513) with the *Bekins* case (394 U. S. 27), it will be seen that only because it is

bottomed upon the principle of composition is the Municipal Bankruptcy Act sustained at all.

See *In re: Nine North Church Street*, 82 F. (2d) 186;
City of West Palm Beach, 96 F. (2d) 85, 86;
Texas Hotel Co. v. Waco Dev. Co., 87 F. (2d) 395;
St. Louis Union Trust Co. v. Champion Shoe Machinery Co., 109 F. (2d) 313.

Assignment No. (6).

The Court of Appeals erred in failing to hold (a) that if the plan sought to be confirmed was the plan of February 1, 1937 (R. 23), it was necessarily not a **plan of composition** within the meaning of the Municipal Bankruptcy Act or Section 83(j) thereof, (b) that if the plan sought to be confirmed was the plan of January 28, 1939 (R. 1), the holders of the "refunding bonds" were not creditors affected by the plan and their consents can not be used to coerce creditors who are affected by the plan and who are in a separate classification.

(a) As stated *supra*, the City of Sanford proposed its original **plan of adjustment** (R. 23) on **FEBRUARY 1, 1937,** at a time when there was no Municipal Bankruptcy Act in existence. That plan, therefore, could not possibly have been a **plan of composition** within the meaning of the Municipal Bankruptcy Act. Moreover, that plan did not contemplate the submission to or approval by any Court and did not contemplate coercion of any non-assenting bondholders. On the contrary, it

contemplated, and was construed and executed as contemplating individual action by each individual bondholder who was permitted to surrender his "old bonds" and to accept and receive his "new bonds" unconditionally, irrevocably and without any reference whatever to the action taken or not taken by the other bondholders. The plan, therefore, was plainly not a **"plan of composition"** and the securities received under it were, therefore, not securities received in partial execution of a **"plan of composition,"** as contemplated by Section 83(j).

(b) After some 87% of the bondholders had accepted the **plan of voluntary adjustment** of February 1, 1937, and had irrevocably and unconditionally surrendered their bonds and accepted the new "refunding bonds" on a scaled-down basis and having different rights and payable from a different fund, the City of Sanford on **JANUARY 28, 1939,** came forward with its so-called **"plan of composition."** This **"plan of composition"** did not and does not in any wise change or alter the rights of the holders of the "refunding bonds." Those "refunding bonds" are, therefore, not "affected by the plan." It does, however, materially change and shrink the rights of the holders of the "old bonds." It undertakes to coerce the holders of the "old bonds" into accepting this shrinkage by having appended to it the consents of the holders of the "refunding bonds." As those holders are not "affected by the plan," they are prohibited by the express language of the statute from having their consents used to coerce the persons who are affected by the plan.

Assignment No. (7).

The Court of Appeals erred in holding

> that Section 83(j) of the Bankruptcy Act (11 U.S.C.A. §403(j)) should not be construed as having retroactive application to securities received and rights abandoned before its adoption.

The settled rule for the interpretation of statutes is that they will not be given a retroactive operation unless it is imperative that no other meaning can be given to them. This Court states this doctrine in *U. S. v. Heth*, 3 Cranch 398, 413, 2 L. Ed. 479, as follows:

> "Words in a statute ought not to have a retroactive operation, unless they are so clear, strong and imperative that no other meaning can be annexed to them, or unless the intention of the legislature cannot be otherwise satisfied."

The Supreme Court of Virginia, in *Crigler v. Alexander*, 33 Gratt. 677, adds to the foregoing statement of law, the following:

> "And although the words of the statute may be broad enough in their liberal extent to comprise existing cases, they must still be construed as applying only to cases that may thereafter arise unless a contradictory intention is unequivocably expressed therein."

The above cases were cited and approved in the case of *Seaboard Steel Casing Co. v. Trigg Co.*, 124 Fed. 75, where the effect of an amendment to the Bankruptcy Act enacted February 5, 1903, was in question. The Court said:

> "This doctrine is definitely accepted by the courts of the United States and of this state. Indeed, the presumption is that statutes are intended to operate prospectively rather than retroactively;

> and they should be so interpreted unless the act itself plainly negatives such a construction. Shreveport v. Cole, 129 U. S. 36, 9 S. Ct. 210, 32 L. Ed. 589; City Ry. Co. v. Citizens Ry. Co., 166 U. S. 557, 17 S. Ct. 653, 41 L. Ed. 1114."

In *8 Corpus Juris Secundum, Bankruptcy*, Section 11, the author says:

> "As a rule, neither the Bankruptcy Act nor the amendments thereto are retroactive in effect, and amendments to the Bankruptcy Act do not apply to cases pending at the time they become effective unless the amendatory acts clearly indicate an intention that they shall apply and then only to the extent indicated."

This Court has recognized the foregoing statement of the doctrine as applied to bankruptcy acts in the case of *Auffmordt v. Rasin*, 102 U. S. 620, 26 L. Ed. 262. There a petition in bankruptcy had been filed on February 5, 1874. The assignee in bankruptcy then sued to recover securities transferred by the bankrupt on November 15, 1873. At the time of the filing of the petition, and at the time of the transfer, the period, prescribed by the act, relating to preferences, was four months. Congress, on June 22, 1874, amended the Act so as to provide a two-months' period. The suit to recover the securities was started after the passage of the amendment and the lapse of two months was set up as a defense. The Court said:

> "It is to be observed that the full period of four months from the receipt of the securities had pased, indeed, more than six months had passed, before the enactment of this amendment, and the bankruptcy proceeding had been initiated within that period and the assignee appointed. **The rights of the parties were therefore fixed before the new**

> **law was passed.** The assignee had a vested right to the securities, or to their value. The defendants were under legal obligation to return these securities or to pay their value to the assignee. To hold that Congress intended by this amendatory statute to take away that right of action is to hold that it intended by a retrospective statute to destroy a vested right of property or an existing right of action. **If it be conceded that Congress could do this, the principle is too well established to need the citation of authorities, that no law will be construed to act retrospectively unless its language imperatively requires such a construction."** (Emphasis ours).

Holt v. Henley, 232 U. S. 637. In this case, an attempt was made to give a retroactive effect to the June 25, 1910, amendment to the Bankruptcy Act. The Court said:

> "Before that amendment, Holt had a better title than the trustees would have got. York Mfg. Co. v. Cassell, 201 U. S. 344, 50 L. Ed. 782, 26 Sup. Ct. Rep. 481. We are of opinion that the Act should not be construed to impair it. We do not need to consider whether or how far in any event the constitutional power of Congress would have been limited. **It is enough that the reasonable and usual interpretation of such statutes is to confine their effect, so far as may be, to property rights established after they were passed.** If, as they sometimes do, the registry statute had fixed a time within which the registration must take place, and the time had elapsed, we think it clear that the amendment would not be read as attempting to diminish Holt's rights. **But the most obvious, if not the only, way of reaching that result, would be by taking the amendment to affect subsequently established rights alone. That is a familiar and natural mode of interpre-**

tation, whereas it would be highly artificial to say that it affected existing rights that still might be secured, but not those for which the chance had been lost. * * * His continuing title simply was postponed to purchasers without notice and creditors getting a lien. We are of opinion that it was not affected by the enactment of later date than the conditional sale. The opposite construction would not simply extend a remedy, but would impute to the act of Congress an intent to take away rights lawfully retained, and unimpeachable at the moment when they took their start." (Emphasis ours).

Arctic Ice Machine Co. v. Armstrong County Trust Co., 192 Fed. 114 (C.C.A. 3rd Cir.):

"It is our opinion, however, that the clause should not receive the construction thus given it. **The contract of sale before us antedates the amendment.** The rights of the vendor and vendee were fixed by it. Under the law of Pennsylvania the reservation of title in the Arctic Ice Machine Company was good from March 22, 1909, the date of the contract of sale, to June 25, 1910, the date of the amendment, against any trustee in bankruptcy that might have been appointed for Keener Brothers. To hold that the amendment divested the vendor of its reserved title is, independent of any constitutional question, to give it a retroactive effect, not consistent with any expressed intent of Congress. The principle is too well established to be disregarded that a statute shall not, except where the legislative intent is clear, be permitted to have a retroactive effect." (Emphasis ours).

The case of *In Re: United States Restaurant & Realty Co.*, 187 Fed. 118, (C.C.A. 2nd Cir.), was an appeal by petitioning creditors from a decree refusing

to adjudicate the United States Restaurant Company a bankrupt. The restaurant company was not subject to the provisions of the Bankruptcy Act as it stood prior to the amendment of June 25, 1910. On April 7, 1910, it made a general assignment for the benefit of creditors. In so doing, as held by the court, it did not commit an act of bankruptcy because the provisions of the act in force at the time of the assignment applied only to persons who might become bankrupts. The amendment of June 25, 1910 (Section 4) for the first time brought the restaurant company within the category of possible bankrupts. The Court held:

> "The sole question in the case is whether by so doing Congress intended that an act done by the corporation which was in no way improper or obnoxious to any provision of statute when it was done should be availed of to send the corporation into the bankruptcy court, when its estate had already been put into a position where it was being administered under the insolvent laws of the state. To hold this would be to give to the amendment a retroactive effect, and we concur with the district judge in the conclusion that there is nothing in the amending statute which requires such a construction. And unless such an intention on the part of Congress is clearly expressed in the act itself, its provisions should not have a retrospective operation. U. S. v. Heth, 3 Cranch 399, 2 L. Ed. 479.
>
> "The appellant contends that the amendment merely enlarges a remedy already existing, and he cites Pond v. N. Y. National Exchange Bank, (D. C.) 124 Fed. 992, where it was held that an act conferring jurisdiction of certain suits on a court which theretofore was without such jursidiction was not confined to rights of action subsequently arising. In that case, however, rights of action theretofore existing could have been en-

forced elsewhere. In the case at bar no creditor of the company had any existing right to throw it into bankruptcy as a consequence of its having made a general assignment."

These cases are only a few of the very numerous authorities which hold that no statute will be construed to act retrospectively unless its language imperatively requires such a construction. Amendment, Sub-section (j), contains no language making it apply to situations created in the past, nor even to cases pending at the time of its adoption. The amendment cannot be construed retroactively. To hold that the petitioner's partially executed **voluntary adjustment** (95% completed) is revived as a **plan of composition** by the amendment will mean that any municipality that at any time in the past has settled a majority of its debts through a voluntary refunding plan can now come into court and use the consents of the holders of refunding bonds to force holders of unrefunding bonds to accept its original plan. This could be even extended to a voluntary plan completely executed 10 or 20 or any number of years ago.

Assignment No. (8).

The Court of Appeal erred in failing to hold that if Section 83(j) of the Municipal Bankruptcy Act be construed as applicable to the case at bar and as authorizing creditors whose rights are unchanged by a **"plan or composition"** to compel acceptance of that plan by creditors whose rights are materially curtailed by that plan, and as authorizing the use on Jan. 28, 1939, for the purpose of determining the solvency or insolvency of the City, the bonds voluntarily

> and irrevocably shrunk on Feb. 1, 1937, not at their shrunken figures, but at the expanded figures existing prior to the voluntary shrinkage, it is null and void as being in violation of the provisions of the Federal Constitution, particularly Amendment V.(1)

If this statute baldly permitted 4,000 holders of bonds of the City of Sanford, each for the principal sum of $1,000, by their votes to compel 240 non-assenting holders of bonds of that City, each for the principal sum of $1,040, to acept a **plan of composition** which simply took the extra $40 away from each of the 240 non-assenting bondholders and gave to each of the 4,240 bondholders identical bonds of $1,000 each, this Court would undoubtedly brand that statute as unconstitutional. Stripped of its confusing detail, that is precisely what the plan now before the Court contemplates doing. At the time that the plan was presented on January 28, 1939, the City of Sanford had outstanding two classes of bondholders, one class who had bonds upon which there was due $1,000 of principal and interest from March 1, 1937, and who were entitled under the law to share in the sinking fund, and another class of bondholders each of whom had a bond for $1,000 bearing interest **from**

(1) Among the cases declaring Acts of Congress void as having violated the Fifth Amendment are the following:
Councilman v. Hitchcock, 142 U. S. 547.
Monongahela Nav. Co. v. U. S., 148 U. S. 312.
Wong Wing v. U. S., 163 U. S. 228.
U. S. v. L. Cohen Grocery Co., 255 U. S. 81.
U. S. v. Moreland, 258 U. S. 433.
Lipke v. Lederer, 259 U. S. 557.
Adkins v. Children's Hospital, 261 U. S. 525.
A. B. Small Co. v. American Sugar Ref. Co., 267 U. S. 233.
Blodget v. Holden, 275 U. S. 142.
Untermeyer v. Anderson, 276 U. S. 440.
Radford v. Louisville Joint Stock Land Bank, 295 U. S. 555.

a date long prior to March 1, 1937, and bearing interest in the future at rates materially higher than the rates borne by the bonds of the class first mentioned. The City of Sanford proposed that by a vote of the holders of the bonds having the lesser amount of rights, the surplus rights above mentioned should be taken away from the second class of bondholders without the consent and over the protest of the holders of the bonds of the class being penalized. If Section 83(j) is construed to permit this treatment, it is, we submit not permissible legislation, but is void as in contravention of the Fifth Amendment.

295 U. S. 589, *Louisville Bank v. Radford:*

> "The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment."

186 U. S. 181, *Hanover Bank v. Moyses:*

> "Congress may prescribe any regulations concerning discharge in bankruptcy that are not so grossly unreasonable as to be incompatible with fundamental law."

R. R. Retirement Board v. Alton R. R., 295 U. S. 330, dealing with the Retirement Act provision in favor of previously discharged railroad employees, the Court said:

> "This clearly arbitrary imposition of liability to pay again for services long since rendered and fully compensated is not permissible legislation. The Court below held the provision deprived the railroads of their property without due process and we agree with that conclusion. Here again the petitioners insist that the requirement is appropriate because they say it does not demand addi-

tional pay for past services, but expenditure 'for a present and future benefit through improvement of the personnel of the carriers'. But the argument ends with mere statement. Moreover, if it were correct in its assumption, which we shall presently show it is not, nevertheless, there can be no constitutional justification for arbitrarily imposing millions of dollars of additional liabilities upon the carriers in respect of transactions long closed on the basis of cost with reference to which their rates were made and their fiscal affairs adjusted."

Caldwell v. Texas, 137 U. S. 692:

"and due process is so secured by laws operating on all alike and not subjecting the individual to the arbitrary exercise of the powers of government unrestrained by the established principles of private right and distributive justice."

Nebbia v. New York, 78 L. Ed. 940, 291 U. S. 502.

"The fifth amendment in the field of federal activity and the fourteenth, as respect state action, do not prohibit governmental regulation for the public welfare. They merely condition the exertion of the admitted power, by securing that the end shall be accomplished by methods consistent with due process, and the guaranty of due process, as has often been held, demands only that the law shall not be unreasonable, arbitrary or capricious, and that the means selected shall have a real and substantial relation to the object sought to be obtained. It results that a regulation valid for one sort of business, or in given circumstances may be invalid for another sort, or for the same business under other circumstances, because the reasonableness of each regulation depends upon the relevant facts."

In re: City of West Palm Beach, 96 Fed. (2d) 85:

> "The binding of a minority by a majority having the same interests was discussed as respects corporate reorganizations in *Texas Hotel Securities Co. v. Waco Development Co.*, (5th Cir.) 87 F. (2d) 395; and *Continental Ins. Co. v. Louisiana Del. Ref. Corp.*, (5th Cir.), 89 Fed. (2d) 333. The importance of identity of interest is there stressed. We do not think the creditors of West Palm Beach who have already irrevocably scaled their debts can be considered either in the two-thirds finally to be needed, nor as preliminary acceptors of the scaling plan offered as a composition."

Continental Ill. Bank & Trust Co. v. C. R. I. & P. Co., 294 U. S. 648:

> "As far back as *Colder v. Ball*, 3 Dell. 386, 1 L. Ed. 648, it was said that among other acts which Congress could not pass was 'a law that destroys or impairs the lawful private contracts of citizens' * * * Speaking generally, it may be said that Congress, while without power to impair the obligation of contracts by laws acting directly and independently to that end, undeniably has authority to pass legislation pertinent to any of the powers conferred by the Constitution, however it may operate, collaterally or incidentally to impair or destroy the obligation of private contracts."

Untermeyer, Executrix v. Anderson, 276 U. S. 440:

> In this case the Court held that the Gift Tax Act adopted by Congress June 2, 1924 was applicable to gifts throughout the year 1924 and that (head note 2): "So far as applicable to bona fide gifts not made in anticipation of death and fully consummated prior to June 2, 1924 these provisions are arbitrary and invalid under the due process clause of the Fifth Amendment."

See also: 275 U. S. 142, *Blodgett v. Holden.*
Columbia Bank v. Okely, 4 Wheat. 244:

> "As to words from Magna Charta incorporated in the constitution of Maryland, after volumes spoken and written with a view to their exposition, the good sense of mankind has at length settled down to this: that they are intended to secure the individual from the arbitrary exercise of the powers of government, unrestrained by the established principles of private rights and distributive justice."

See also:

75 Fed. 2d 256, *Re. Central Funding Corporation,* (C. C. A. 2).
75 Fed. 2d 947, *Campbell v. Allegheny Corp.,* (C. C. A. 4).

10 Fed. Sup. 776, *Re Pierce Arrow Sales Corp.*

The obligations sought to be impaired are obligations of a subdivision of the State. The Court, we are sure, has in mind that the obligations sought to be shrunk without the consent of their holders are the obligations of a municipal corporation and has in mind that in the *Ashton* case, 298 U. S. at 531 it said:

> "If obligations of States or their political subdivisions may be subjected to the interference here attempted, they are no longer free to manage their own affairs; the will of Congress prevails over them; although inhibited, the right to tax might be less sinister. And really the sovereignty of the State, so often declared necessary to the federal system, does not exist. McCulloch v. Maryland, 4 Wheat. 316, 430. Farmers & Mechanics Bank v. Minnesota, 232 U. S. 516, 526.
>
> "The Constitution was careful to provide that 'No State shall pass any Law impairing the Obligation of Contracts.' This she may not do under

> the form of a bankruptcy act or otherwise. Sturges v. Crowninshield, 4 Wheat. 122, 191. Nor do we think she can accomplish this same end by granting any permission necessary to enable Congress so to do."

and that it in that decision proceeded to hold unconstitutional the original Municipal Bankruptcy Act.

The Court will moreover undoubtedly have in mind the fact that it thereafter affirmed the constitutionality of the Second Municipal Bankruptcy Act in the *Bekins* case, 304 U. S. 27, and that in the course of its opinion, the following occurred. On page 49, the Court said:

> "**Third.** We are thus brought to the inquiry whether the exercise of the federal bankruptcy power in dealing with **a composition of the debts of the irrigation district,** upon its voluntary application and with the State's consent, must be deemed to be an unconstitutional interference with the essential independence of the State as preserved by the Constitution."

The Court then referred to the *Ashton* case and thereafter quoted at length from the report of the Congressional Committee, which strongly stressed the fact that the new statute was bottomed on a composition, which in turn was bottomed on the consents of 51% of the creditors affected by the plan. Thereafter on page 51, the Court said:

> "We are of the opinion that the Committee's points are well taken and that Chapter X is a valid enactment. The statute is carefully drawn so as not to impinge upon the sovereignty of the State. The State retains control of its fiscal affairs. The bankruptcy power is exercised in relation to a matter normally within its province and **only in a case** where the action of the taxing agency in **carrying**

> **out a plan of composition** approved by the bankruptcy court is authorized by state law. It is of the essence of sovereignty to be able to make contracts and give consents bearing upon the exertion of governmental power."

Thereafter on page 54 the Court said:

> "Fourth. As the bankruptcy power may be exerted to give effect to a plan **for the composition of the debts of** an insolvent debtor, we find no merit in appellant's objections under the Fifth Amendment. In re Reiman, *supra;* Continental National Bank v. Chicago, R. I. & P. Ry. Co., *supra.*"
>
> (All emphasis in above quotations by present writers).

All of this emphasizes the fact that in order for the statute to be constitutional, the consent of the majority of the creditors affected by the plan must be secured. In the case at bar, not one single creditor affected by the plan has given his consent. The consents by which the affected creditors are sought to be coerced are consents of creditors whose interests are not affected by the plan.

So, too, if the statute baldly permitted bondholders participating in a discussion of the solvency or insolvency of a City held on January 28, 1939, to be counted for the purpose of determining such solvency or insolvency, not at the amounts which were due them by the City on January 28, 1939, but at the amounts which were due them by the City on February 1, 1937, although the amounts due February 1, 1937, were materially larger than the amounts due January 28, 1939, this Court would undoubtedly brand that statute unconstitutional. That, however, is in substance what is being sought to be done here, since the action gives those "refunding

bondholders" rights to which they are not entitled and takes away from the "old bondholders" rights to which they are entitled. Those "old bondholders" are here before the Court contending that the statute as thus construed deprives them of due process, in violation of the provisions of the Constitution of the United States.

All of which is respectfully submitted.

AMERICAN NATIONAL BANK
OF NASHVILLE, TENNESSEE,
By GEORGE W. WYLIE,
STUART B. WARREN,
F. A. BERRY,
J. BLANC MONROE,
MONTE M. LEMANN,
Attorneys for Petitioner.

WYLIE & WARREN,
BASS, BERRY & SIMS,
MONROE & LEMANN,
Of Counsel.

August, 1940.